

PT 05-26

Tax Type: Property Tax

Issue: Charitable Ownership/Use

**STATE OF ILLINOIS
DEPARTMENT OF REVENUE
OFFICE OF ADMINISTRATIVE HEARINGS
CHICAGO, ILLINOIS**

CONDELL MEDICAL CENTER,

Applicant

v.

**THE DEPARTMENT OF REVENUE
OF THE STATE OF ILLINOIS**

**No. 04-PT-0004
103-49-87
103-49-86**

**Charles E. McClellan
Administrative Law Judge**

RECOMMENDATION FOR DECISION

Appearances: John D. Alshuler, Special Assistant Attorney General, for the Illinois Department of Revenue (the “Department”); Mr. James S. Levi of Hodges, Loizzi, Eisenhammer, Rodick & Kohn for Antioch Community High School District 117 and Round Lake School District No. 116 (“Intervenors”); and Craig J. Donnewald of Finkel, Martwick & Colson for Applicant.

Synopsis:

This matter involves partial non-homestead exemptions granted by the Department for each of two parcels of property owned by Medical Center Properties, Inc. that is an affiliate of Condell Medical Center. Medical Center Properties, Inc. is organized solely to hold ownership of properties such as the two parcels involved in this matter. Following the granting of partial exemptions by the County Board of Review for each parcel, on November 30, 2003 the Department issued a Non-Homestead Property Exemption Certificate for the identified portions of each of these parcels for the

assessment year 2003. Interveners filed requests for formal hearings to contest the exemptions on January 14, 2004. The matters were consolidated for hearing. The parties stipulated to certain facts that are identified in the record as Department Group Exhibit No. 2. A hearing was held on February 16, 2005.

I recommend that the Department's previous grant of the partial two exemptions be reversed and that the exemption applications be denied.

Findings of Fact:

1. The properties that are the subject of this consolidated matter are the following:

Two East Rollins Road, Round Lake Beach, Avon Township, Lake County, Illinois assigned PIN 06-100-029-0000. ("Round Lake").

317 East Grand Avenue, Lake Villa, Lake Villa Township, Lake County, Illinois assigned PIN 06-04-104-029-0000. ("Lake Villa").
Dept. Group Exs. No. 1 & 2, Tr. p. 10.

2. Round Lake and Lake Villa are legally and beneficially owned by Medical Center Properties, Inc. Dept. Group Ex. No. 2.
3. Medical Center Properties, Inc. is an affiliate of Applicant, and is organized solely to hold ownership of Round Lake, Lake Villa and other similar facilities for the use and benefit of Applicant. *Id.*
4. Through its affiliate, Medical Center Properties, Inc., Applicant has had interests amounting to ownership in both Round Lake and Lake Villa since prior to January 1, 2003 and continues to own these properties. *Id.*
5. Round Lake is improved with a two-story medical office building containing 21,403 usable square feet. *Id.*

6. Of the total usable square feet in the Round Lake building, about 6,080 square feet in the basement and on the first floor, comprising about 28% of the building's total usable square feet, are used by Applicant for an Acute Care Center. The rest of the usable square footage is leased to medical office tenants who are affiliated with Applicant. *Id.*
7. Lake Villa is improved with a two-story medical facility containing 10,735 usable square feet. *Id.*
8. Of the total usable square feet in the Lake Villa building, about 3,118 on the second floor, comprising about 29% of the building's total usable square feet, are used by Applicant as a Physical Therapy Center. The rest of the usable square footage is leased to medical office tenants who are affiliated with Applicant. *Id.*
9. During 2003, both the Acute Care Center at Round Lake and the Physical Therapy Center at Lake Villa were staffed by Applicant's employees. During that year, the fee schedules and collection policies for services rendered by Applicant's employees at Round Lake and Lake Villa were substantially the same as those in effect at Applicant's primary facilities in Libertyville, Illinois as well as at Applicant's other area facilities. *Id.*
10. The Department of Revenue has adjudicated Applicant's primary facilities as exempt from real estate taxation, either in whole or in part, since at least the early 1990's, as evidenced by Illinois Department of Revenue Exemption Certificate Nos.:

91-49-25	91-49-26	93-49-96	94-49-289
94-49-290	94-49-291	94-49-292	94-49-293

11. Applicant is a Not-For-Profit Corporation organized under the Laws of the State of Illinois prior to January 1, 2003. *Id.*
12. Applicant is an organization described in Internal Revenue Code § 501(c)(3), 26 USC § 501(c)(3), that is exempt from federal income tax, and is qualified to accept deductible charitable contributions from the general public. Applicant is also a public charity as described in Internal Revenue Code § 509(a)(1), 26 USC § 509(a)(1). Tr. pp. 119-120.
13. The compensation paid to Applicant's employees is consistent with the level of compensation paid by other hospital facilities as determined by its personnel department on the basis of hospital compensation surveys. *Id.*, Tr. p. 136.
14. Applicant provides certain managers with bonuses that can be up to 7% of a manager's salary. The amounts of the bonuses are determined by Applicant's personnel department to keep it in line with what similar hospitals are paying. Tr. pp. 135-136.
15. Applicant's purpose as set forth in its bylaws is to operate a hospital and other health care facilities and to conduct activities that promote the general health of residents of the community. Applicant also conducts lectures and sponsors support groups that conduct meetings that are generally free of charge and deal with health and wellness subjects. It distributes free publications regarding health and wellness subjects. It donated automated electronic defibrillators to various police departments in the community. It provides discounted flu vaccinations,

- mammograms, and other medical services. It sponsors internship programs for various medical specialty technicians. It also provides free meeting space for local community organizations. Tr. pp. 121-129, Applicant Ex. No. 14.
16. On November 20, 2003, the Department granted Non-homestead Property Tax Exemption Certificate No. 03-49-89 for 28% of Round Lake for the assessment year 2003. Dept. Ex. No. 1.
 17. On November 20, 2003, The Department granted Non-homestead Property Tax Exemption Certificate No. 03-49-87 for 29% of Lake Villa for the assessment year 2003. *Id.*
 18. Applicant has patient intake and patient billing policies and procedures that are applied uniformly throughout Applicant's facilities including the Round Lake and Lake Villa facilities. Tr. pp. 13-14.
 19. When a patient arrives at one of Applicant's facilities under Applicant's intake procedure the patient is registered by obtaining his or her personal identification information, either before service is rendered in the case of a scheduled procedure or after service is rendered in the case of an emergency room admittance. Tr. pp. 15-20.
 20. During the registration process, Applicant determines if the patient has medical insurance. *Id.*
 21. Applicant has a Financial Assessment Policy to be followed by the interviewer at the patient's registration. Applicant's assessment procedure is designed to determine the patient's insurance coverage, possible government coverage, who is liable, as, for example, in the case of an automobile accident, and ability to pay if

- there is no insurance coverage. The assessment procedure is required by the federal government to determine who will be primarily responsible for the cost of the patient's medical care. Tr. pp. 35-37, Applicant Ex. No. 3.
22. In appropriate situations, as when a patient has no insurance, Applicant's interviewers utilize a checklist to request from the patient the documents that are necessary to determine a patient's Public Aid or Medicaid eligibility. Tr. pp. 37-39, Applicant Ex. No.4.
23. If a patient does not have insurance and does not qualify for public aid or charity because the patient's income level is too high, Applicant offers self-pay options. Applicant has a Self-Pay Option Policy and a Self-Pay Discount Policy to be followed by its collectors and its financial counselors in negotiating payment plans for self-pay patients. Tr. pp. 40-44, Applicant Ex. Nos. 5, 6,
24. If the Self-Pay options do not apply to a patient because of indigence, Applicant has a Financial Assistance Program under the terms of which the patient is offered discounts on a sliding scale depending on the patient's income. Tr. pp. 47-51, Applicant Ex. No. 7.
25. Applicant has a packet of forms it uses in cases where a patient has requested financial assistance in paying Applicant's bill. The documents in this packet are printed in Spanish and English because Applicant has a high number of Spanish speaking patients. The documents request detailed statements of assets, liabilities, income sources, expenses, and employment data. Tr. pp. 51-59, Applicant Ex. No. 8.

26. Applicant may grant percentage discounts on a sliding scale depending on its evaluation of the patient's ability to pay. If Applicant determines that a patient's financial situation does not warrant financial assistance, it will be denied. *Id.*
27. Applicant's procedure for financial evaluation is set forth in a document that is sent to all of Applicant's facilities. It includes a schedule showing the Federal poverty guidelines, that is updated annually, and is mandated by the federal government for hospitals and healthcare facilities to use in evaluating patients' qualification for free or reduced fee services. Tr. pp. 59-61, Applicant Ex. No. 9.
28. In obstetric cases, Applicant normally expects payment in full for delivery at the time of discharge. If a pregnant woman comes in off the street in labor and requires immediate care but has no insurance but has the ability to pay, payment arrangements can be made. If she has no ability to pay she would qualify for Medicaid. Tr. pp. 72, 77, Applicant Ex. No. 6.
29. Patients always receive the medical treatment they need whether or not they have insurance or the ability to pay. No patient needing treatment has ever been turned away for lack of ability to pay. Tr. pp. 15-20, 65-71, 116.
30. When a patient is discharged, the medical services rendered are entered into Applicant's billing system and coded. Then a bill is sent to the patient. Applicant's billing form advises patients that financial aid is available, but Applicant does not advertise that charitable medical services are available. Tr. pp. 20-21, 73 Applicant Ex. No. 2.

31. Thirty days after the bill is sent out a statement of account is sent to the patient. Thirty days after that statement a third statement is sent to the patient. Tr. pp 21-22.
32. After the second statement, the account is referred to Computer Credit Incorporated that sends out a series of three different letters to the patient, two weeks apart. Each letter gets more detailed or asks for more information, or asks the patient to contact Applicant to make payment arrangements. Tr. p. 22.
33. For the year 2003, Applicant's gross revenue was \$630 million. Applicant's net revenue for that year after write-offs for contractual discounts for PPOs, HMOs, Medicare and Medicaid was \$230 million. Tr. pp. 86-87, 105-106, Applicant Ex. No. 10.
34. During 2003, Applicant's net income after expenses was about \$15 million or \$16 million. It's actual charity write-offs, for charity patients who could not afford to pay, were \$295,695. Tr. p. 104.
35. During 2003, Applicant received a \$732,000 contribution from the hospital auxiliary representing proceeds from fundraisers it conducted, \$45,000 in contributions from unrelated corporations, and \$155,437 in contributions from individuals. Tr. pp. 112-115. Applicant Ex. No. 13.
36. Of the \$932,737 in total contributions received during 2003, about \$20,000 to \$30,000 was designated for charity care. Tr. p. 133.
37. During 2003, Applicant also received grants of \$8,871 and \$79,800 from the State to reimburse it for the cost of disaster drills it conducted and disaster preparedness expenses; and it received a \$200,000 grant from the Health Resources Services

Administration to help Applicant set up its brain and spine program to treat neurological cases. Thus, the total of contributions and grants received during 2003 was \$1,221,108. *Id.*

38. Applicant's normal pricing for Public Aid Medical services provided during the year 2003 was \$46,071,895. However, under the contracts Applicant had with the Illinois Department of Public Aid and Medicaid, Applicant had to write off \$41,061,587, so the actual revenue generated from these contracts was \$5,010,308, which was \$9,816,488 less than the cost's Applicant incurred in providing those services. Tr. pp. 85-87, 100-106, Applicant Ex. No. 10.
39. In 2003, Applicant treated in excess of 100,000 patients of whom 84 were charity patients. *Id.*
40. During 2003, 13% of Applicant's patients were Public Aid patients and 3½ % were low-income patients on Medicare, so the total of 16½ % exceeded the minimum of 15% required to qualify for the Federal Disproportionate Share Program that provides a bonus from the federal government that is added to its Medicare reimbursements. Tr. p. 91-92.
41. Because of the large number of Public Aid and low-income patients treated by Applicant during the years 2001, 2002, and 2003, Applicant qualified for the Federal Disproportionate Share Program for all three years. *Id.*
42. Any income left at the end of the year stays within the hospital and is used for capital improvement, to buy equipment or to subsidize services. For example, in the last three years, Applicant spent \$120 million on a capital expansion project that added a new state of the art intensive care ward, a state of the art emergency

- room, a linear accelerator to use noninvasive methods to treat more advanced cancers, and a scanner for diagnosing cancer. Tr. pp. 98, 119.
43. Applicant's Rehabilitation Services Center at its Lake Villa facility provides physical, occupational, and speech therapy services to patients of all ages in the community. Referrals are accepted across the continuum from acute care, sub-acute care, home-health or community sources without discrimination on the patients' ability to pay. Tr. pp. 130-132, Applicant Ex. No. 15.
44. Applicant's Acute Care Center at its Round Lake facility provides medical and educational services to patients of all ages in the community. It provides services for minor injuries and illnesses, occupational health services and outpatient laboratory and radiology services. It meets the educational needs of the community by providing blood pressure screenings, diabetic screenings, thyroid screenings, drug screenings and flu vaccinations. It provides occupational and educational services in conjunction with local colleges and other services as well. It also does not discriminate on the basis of patients' ability to pay *Id.*
45. For the year 2003, Lake Villa realized net income of about \$60,000 from total revenue of \$1,426,932. Tr. p. 95, Applicant Ex. No. 12.

Conclusions of Law:

The testimony and exhibits in the record establish that Applicant is not entitled to the partial exemptions from 2003 real estate taxes previously granted by the Department under Section 15-65(a) of the Property Tax Code¹. Therefore, for the reasons set forth below, I recommend that the Department's partial exemptions (28% of Round Lake and 29% of Lake Villa) be denied.

Article IX, Section 6 of the *Illinois Constitution of 1970* gives the General Assembly the authority to grant property tax exemptions in limited circumstances as follows:

The General Assembly by law may exempt from taxation only the property of the State, units of local government and school districts and property used exclusively for agricultural and horticultural societies, and for school, religious, cemetery and charitable purposes.

Acting under the authority granted by the Constitution, the General Assembly enacted a statute exempting certain charitable organizations which, in relevant part, provides as follows:

§ 15-65. Charitable purposes. All property of the following is exempt when actually and exclusively used for charitable or beneficent purposes, and not leased or otherwise used with a view to profit:

(a) Institutions of public charity. 35 ILCS 200/15-65(a).

In summary, in the context of this case, the statute requires that (1) the property be owned by an entity that qualifies as an “institution of public charity;” and, (2) the property be actually and exclusively used for charitable purposes.” *Id*; *Methodist Old People's Home v. Korzen*, 39 Ill.2d 149, 156, 157, 233 N.E.2d 537 (1968).

In *Methodist Old People's Home* the Supreme Court set forth six requirements for ownership and use that an organization must satisfy to be entitled to exemption. These requirements are as follows:

1. The organization must benefit an indefinite number of persons, persuading them to an educational or religious conviction, for their general welfare, or by reducing the burdens of government in some other way.
2. The organization cannot have capital stock or shareholders, earn any profits, or pay dividends.

¹ 35 ILCS 200/1-1 *et seq.*

3. The organization must derive its funds mainly from public and private charity and hold them in trust for the objects and purposes expressed in its charter.
4. The organization must dispense charity to all who need and apply for it.
5. The property must be actually and factually used exclusively for charitable purposes, regardless of any intent expressed in the organization's charter or by-laws.
6. The organization must use its facilities exclusively for the charitable purposes for which it was formed which means that its use must be primarily for that purpose. *Eden Retirement Center, Inc. v. Dept. of Revenue*, 2004 WL 2745641 (December 2, 2004), *Methodist Old People's Home*, 39 Ill.2d at 157.

Applicant claims partial exemption for the portion of Lake Villa that it uses as its Physical Therapy Center and that portion of Round Lake that it uses for its Acute Care Center under Section 15-65 (a) of the Property Tax Code. 35 ILCS 200/15-65(a). The parties' dispute with respect to the portions of the parcels at issue is whether Applicant has met the tests set forth in *Methodist Old People's Home* to qualify for charitable exemptions.

Applicant argues that it is entitled to the exemptions initially granted by the Department because of the substantial write-downs it takes on services provided to Public Aid and Medicaid patients and the contractual discounts it provides to patients covered by PPOs, HMOs, Medicare, and others, as well as for the discounts it provides to patients who are unable to pay for the services they receive by insurance coverage or otherwise. Applicant also cites the activities and services it provides to the community. Finally, it cites the exemption certificates that have previously been granted to it by the Department.

The Interveners assert that the write-downs do not constitute charity and that the amount of charity care Applicant dispenses is incidental to the amount of care it provides for fees.

To qualify for a property tax exemption, Applicant must satisfy the requirements set forth by the Supreme Court in *Methodist Old Peoples Home, supra*. With regard to the first rule, Applicant does benefit an indefinite number of people by providing medical care for an indefinite number of people. With regard to the second requirement, Applicant does not have any capital stock or shareholders, and it does not pay dividends. It pays its employees on a scale comparable to other hospitals in the area. It also pays bonuses to its management personal that can range up to 7% of their compensation. The record does not describe the method or procedure by which bonuses are granted in individual cases. However, in the for-profit business world, bonuses are usually awarded for contributions made toward profitability. If that is the case here, it is not consistent with being a charitable operation.

In 2003 Applicant made a profit of \$15 million to \$16 million. That factor violates the second requirement set forth by the Supreme Court. However, this alone might not, by itself, negate an exemption considering that it invested the profits in its facilities. But this level of profit is not consistent with the provision of charity if these substantial funds are not applied toward expanding acts of charity, but, rather, are used to expand services to persons who pay for them. See *Riverside Medical Center v. Dept. of Revenue*, 342 Ill.App.3d 603, 795 N.E.2d 361 (3rd Dist. 2003).

With regard to the remaining tests, the factual pattern in this case is very similar to the factual pattern in *Riverside Medical Center* in which the Applicant sought exemption for three of its clinics. In that case, the court found that the Applicant's clinics did not qualify for exemption.

The third test requires that the organization must derive its funds mainly from public and private charity. A review of the factual pattern in *Riverside Medical Center* is instructive. In that case, the record shows that Riverside derived 97% of its revenues for the year at issue from patient billings. Only 0.05% came from donations, and no grants or donations were made directly to the clinics at issue. Furthermore, the record did not show whether any part of the donations that were made were used for the benefit of the clinics at issue. The court held that these facts did not favor Riverside's position.

In this case, Applicant's gross revenues for 2003 were \$630 million. Applicant's net revenues, after write-offs required by its contracts with HMOs, PPOs, Medicare and Medicaid, was \$230 million. It received contributions and grants of \$1,221,108 during that year. \$1,221,108 is less than 1% of its \$630 million in gross revenues. The contributions and grants were about 0.53% of its \$230 million dollars of revenue after the discounts it granted under its contractual obligations. The fact that Applicant receives substantial sums from sources other than donations and grants does not necessarily cause it to lose its character because some of the recipients of its benefits are able to pay for its services. *Wyndemere Retirement Community v. Dept. of Revenue*, 274 Ill.App.3d 455, 654 N.E.2d 608 (2nd Dist. 1995); *People ex rel. Cannon v. Southern Illinois Hospital*, 404 Ill. 66, 88 N.E.2d 20 (1949). However, in this case, the amount of funds that Applicant received from public and private charity was miniscule. Most of its revenue is derived from fees received for medical services provided to its patients. For the year 2003, Applicant received a much higher percentage of its revenue from fees than did Riverside. Applying the rationale of the court in *Riverside* to the facts of this case demonstrates that Applicant fails the third test.

The fourth test requires Applicant to dispense charity to all who need and apply for it. Applicant also falls short on this requirement. Again reference to *Riverside* is instructive. *Riverside* argued that it did not perform any pre-care screening to determine whether a patient could afford to pay for his or her bill, that its clinics gave the same care to all patients, regardless of ability to pay and that the clinics did not turn patients away.

In analyzing these facts, the court referred to the cases of *Highland Park Hospital v. Dept. of Revenue*, 155 Ill.App.3d 272, 507 N.E.2d 1331 (2nd Dist. 1987) and *Alivio Medical center v. Dept. of Revenue*, 299 Ill.App.3d 647, 702 N.E.2nd 189 (1st Dist. 1998). In *Highland Park*, the hospital gave free care, as did *Riverside*. All patients were seen by a doctor without any screening regarding the ability to pay. The patient was billed after the visit. After 90 days, the bill was classified as uncollectible and written off as free care if the patient was unable to pay. In *Highland Park Hospital*, the hospital wrote off approximately 6% of its care in this way. *Highland Park Hospital, supra*, 155 Ill.App.3d at 276, 507 N.E.2d at 1334.

In *Alivio*, the clinic charged each patient the full price of services following the visit but reduced the amount of the bill if the patient was not able to pay after a number of bills had been sent. *Alivio* wrote off about 25% of its billings as charitable care.

In both *Highland Park* and *Alivio* the court found that the clinics were not giving charity care but were writing off bad debts. In both cases, the court found it relevant that the applicants did not advertise that charity care was available. The *Riverside* court concluded that *Riverside* was doing the same thing, so it also failed the fourth test.

In Applicant's case, the facts are quite similar to *Riverside*, *Highland Park Hospital*, and *Alivio*. Unlike the practices of the facilities in those cases, except in the

case of emergencies, Applicant conducts extensive pre-screening to determine if the patient has insurance coverage or is eligible for Medicaid. If a patient has no insurance or is not eligible for Medicaid, its financial counselors determine the level of payment the patient can afford under its self-pay options. If the self-pay options do not apply because of the patient's indigence, the patient is offered discounts on a sliding scale.

Once a patient is discharged from one of Applicant's facilities it sends the patient a bill for the services rendered. The bill advises the patient that financial assistance is available but it does not advertise that charity is available. After the second bill is sent out, the account is referred to an outside firm to pursue collection. The record in this case does not indicate what happens if the outside firm is not successful in its efforts. It does show, however, that Applicant's write-offs for charity were \$295,695. This amounts to 1% of its \$16 million net profits for the year and less than 1% of its \$630 million gross revenue for the year. Applicant's charity write-offs were far less than those in *Riverside*, *Highland Park*, or *Alivio*.

Applying the rationale of *Riverside*, *Highland Park*, and *Alivio* to the facts of this case establishes that Applicant's facilities were not giving charity, but, rather, were writing off bad debts. Therefore it was not providing charity to all who need it, so it failed the fourth test.

The remaining tests are whether the two facilities at issue were actually used primarily for charitable purposes. Although Applicant's by-laws restrict it to charitable uses, they must also be operated for that purpose. *Riverside Medical Center*, *supra*, 342 Ill.App.3d at 609, 795 N.E.2d at 366. In *Riverside Medical Center*, the Riverside system provided 3% of its budget to charity care and for the year at issue, it ran a deficit of

\$850,000. In this case, the record does not show what percent of Applicant's budget was for charity. However, during 2003, out of more than 100,000 patients served, only 84 of Applicant's total number of patients were charity patients. As for the individual facilities at issue, Lake Villa realized net income of about \$60,000 from total revenue of \$1,426,932. The record does not contain the financial results of operations during 2003 for Round Lake. These factors demonstrate that Applicant used the two facilities at issue primarily for the purpose of providing care to paying patients.

Applicant argues that charity is not limited to free care. Applicant argues that the discounts given to large insurance companies, HMOs PPOs, Medicare and Medicaid should be considered as charity. As the court found in *Riverside*, these discounts are given pursuant to contracts with the underlying organizations. They are not charity. *Riverside Medical Center, supra*, 342 Ill.App.3d at 610, 795 N.E.2d at 366. These facts demonstrate that Applicant's facilities were not actually used primarily for charity. The primary use was to provide care to those patients who could pay for it, either through insurance or otherwise.

For the reasons set forth above, I recommend that the Department's previous grant of the partial two exemptions be reversed and that the exemption grant applications be denied.

Date: 5/11/2005

Charles E. McClellan
Administrative Law Judge